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No. 97-1444

In the Supreme Court of the United States

OCTOBER TERM, 1997

RUSSELL MCLAUGHLIN, JR., ET AL., PETITIONERS

v.

UNITED STATES OF AMERICA

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

SETH P. WAXMAN
Solicitor General
Counsel of Record
LORETTA C. ARGRETT
Assistant Attorney General
ROBERT E. LINDSAY
ALAN HECHTKOPF
WILLIAM A. WHITLEDGE
Attorneys
Department of Justice
Washington, D.C. 20530-0001
(202) 514-2217

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QUESTIONS PRESENTED

1. Whether it was plain error to convict petitioner Mark McLaughlin on an indictment charging him with attempting "to evade and defeat the payment of" income taxes in violation of 26 U.S.C. 7201, where he claimed that the evidence at trial showed at most an attempt to evade the assessment, rather than the payment, of taxes.

2. Whether 26 U.S.C. 7609, which requires a taxpayer to be notified when the Internal Revenue Service seeks documents from a third-party recordkeeper by an administrative summons, prohibits the IRS from obtaining documents from a taxpayer's accountant voluntarily and without a summons.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 7a-35a) is reported at 126 F.3d 130. The district court's pretrial order denying various motions (Pet. App. 46a-62a), including the motion to dismiss the indictment because of the IRS's alleged failure to use an administrative summons to obtain documents (Pet. App. 58a), is reported at 910 F. Supp. 1054. The district court's post-trial order denying various motions (Pet. App. 36a-45a) is unreported.

JURISDICTION

The judgment of the court of appeals (Pet. App. 5a-6a) was entered on September 11, 1997. A petition for rehearing was denied on December 3, 1997. Pet. App.

3a-4a. The petition for a writ of certiorari was filed on March 3, 1998. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

After a jury trial in the United States District Court for the Eastern District of Pennsylvania, both petitioners were convicted on one count of willfully attempting to evade the 1988 federal income tax liability of Buildings Inspection Underwriters, Inc. (BIU), in violation of 26 U.S.C. 7201. Petitioner Russell McLaughlin, Jr., was also convicted on one count of subscribing and filing a false income tax return for BIU, in violation of 26 U.S.C. 7206(1). Both petitioners were acquitted on one count of conspiracy to defraud the United States, in violation of 18 U.S.C. 371. [1] Both petitioners were sentenced to 24 months' imprisonment, to be followed by three years' supervised release, and each was fined $100,000. Pet. App. 8a-9a. The court of appeals, after holding that evidence had been introduced at trial in violation of petitioner Russell McLaughlin, Jr.'s, Fifth Amendment privilege against compelled self-incrimination (Pet. App. 9a-16a), vacated his conviction and remanded for a new trial (*id.* at 28a); he has not yet been retried. The court of appeals also vacated the sentence imposed on petitioner Mark McLaughlin, and remanded for resentencing (*ibid.*); Mark McLaughlin has not yet been resentenced.

1. Petitioners and their relatives own Building Inspection Underwriters, Inc. (BIU), a corporation that conducts building inspections. During 1988, BIU

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[1] Petitioners' sister Robin McLaughlin, who was charged in the conspiracy count only (Pet. App. 63a-71a), was also acquitted.

opened two bank accounts and deposited into each of them more than $700,000 in corporate receipts. Petitioners concealed the existence and nature of those receipts from BIU's accountant; as a result, those amounts were not reported as income on the corporate tax return. Pet. App. 8a; Gov't C.A. Br. 16-17. During the course of an Internal Revenue Service (IRS) tax fraud investigation of BIU's 1988 tax return, BIU's accountant voluntarily provided corporate documents to the IRS. Pet. App. 18a-19a, 52a.

Petitioners were charged in a three-count indictment, Count 2 of which (Pet. App. 72a) alleged that petitioners, in violation of 26 U.S.C. 7201,

> willfully attempted to evade and defeat the payment of a large part of the income tax due and owing by Building Inspection Underwriters Inc. ("BIU") to the United States for the calendar year 1988, by concealing and attempting to conceal from BIU's accountants and the Internal Revenue Service the nature and extent of BIU's income and the location thereof, and by making false statements to BIU's accountant with respect to the nature and extent of BIU's income.

Petitioners moved to suppress the records obtained from their accountant. They contended that 26 U.S.C. 7609 requires the IRS to use an administrative summons to obtain a taxpayer's documents from a third-party recordkeeper and to provide notice of the summons to the taxpayer, even if the taxpayer's accountant is willing to provide records to the IRS voluntarily. The district court denied that motion; it held that "[t]here is no requirement that the IRS issue a summons every time it receives records from third parties," and observed that petitioners' "reading

of the statute would prevent the IRS from conducting informal investigations and mandate court intervention every time an agent seeks documents from anyone, no matter how willing to provide them that person may be." Pet. App. 58a.

2. The court of appeals vacated petitioner Russell McLaughlin's convictions on grounds not pertinent here, and remanded for a new trial. Pet. App. 9a-16a. The court of appeals also vacated petitioner Mark McLaughlin's sentence on grounds not pertinent here, and remanded for resentencing. *Id.* at 24a-28a. The district court has not yet retried petitioner Russell McLaughlin and has not yet resentenced petitioner Mark McLaughlin.

The court of appeals rejected petitioners' contention, raised for the first time on appeal, that there was a failure of proof at trial on Count 2. Petitioners argued that they had been charged with attempting to evade the *payment* of taxes, but the evidence showed at most that they had attempted to evade the *assessment* of taxes. The court first observed that, because that claim had not been presented to the district court, "plain error analysis applies." Pet. App. 16a. It then stated that 26 U.S.C. 7201 includes two distinct offenses, evading assessment of taxes and evading payment of taxes, but that the two offenses "frequently overlap" in their proof. Pet. App. 17a. The court suggested that, if petitioners had been charged only with evasion of payment, the government would have had to prove a valid assessment of the taxes due. But, the court concluded, the government's proof of evasion of assessment did not amend the indictment, which was sufficiently broad to put petitioners on notice that the government was proceeding under an evasion-of-assessment theory. *Ibid.* And in rejecting

the argument that there was a prejudicial variance between the indictment and the proof, the court found that (1) the indictment as a whole made it clear that the government was charging evasion of assessment, (2) petitioners' defense attorney addressed the issue of evasion of assessment at trial, and (3) Count 2 charged conduct that was relevant only to an evasion of assessment charge. *Ibid.*

The court of appeals also affirmed the district court's conclusion that the IRS was not required to issue an administrative summons to obtain information from BIU's accountant, who voluntarily turned over the records in his possession to the IRS. The court assumed that, if the IRS had issued a summons to the accountant, the IRS would have been required by 26 U.S.C. 7609(a) to give notice of that summons to BIU. The court concluded, however, that Section 7609 does not require the use of a summons whenever third parties give the IRS evidence voluntarily. It noted that, under 26 U.S.C. 7602, the IRS has broad discretion in the conduct of its investigations, and that the IRS is expressly authorized to conduct informal investigations. Section 7602(a), it stated, "permits the government to conduct a formal investigation and issue summonses or to proceed informally," and thus the IRS was entitled to proceed informally and request information from petitioners' accountant without informing petitioners. Pet. App. 19a-20a.

ARGUMENT

1. Petitioners' challenges to their indictment and to the use of evidence obtained from their corporate accountant are not ripe for review by this Court. Both petitioners' cases are currently in an interlocutory posture. Petitioner Russell McLaughlin, Jr., will have an opportunity to present his contentions again at his retrial. If he is acquitted following his retrial, then his contentions will be moot. If he is convicted and his conviction is affirmed on appeal, he will then be able to present his contentions, together with any other claims he may have, to this Court in a petition for a writ of certiorari seeking review of the final judgment against him. Similarly, petitioner Mark McLaughlin has not yet been resentenced, and therefore there is no final judgment of conviction against him. He too can seek review of the rulings of the court of appeals, together with any other contentions he may have that might arise upon the remand, after his conviction becomes final and his sentence is affirmed. Accordingly, even if petitioners' contentions had merit, this Court's review of the decision of the court of appeals is unwarranted.

2. Petitioners argue (Pet. 12-20) that they were charged only with evasion of *payment* of taxes but were convicted on proof, at most, only of evasion of *assessment* of taxes. As the court of appeals observed, however (Pet. App. 16a), because petitioners failed to raise that contention in the district court, their claim may be reviewed only for plain error. See Fed. R. Crim. P. 52(b); *United States* v. *Olano*, 507 U.S. 725 (1993). There was no plain error in this case; if any error occurred at trial, it was not "plain," and

petitioners have not shown that they were prejudiced by any error. See *id.* at 734.

Section 7201 creates the offense of attempted tax evasion. Its elements consist of (1) willfulness, (2) a tax liability, and (3) an affirmative act constituting an attempt to evade or defeat the tax or its payment. *Sansone* v. *United States*, 380 U.S. 343, 351 (1965). An individual may attempt to defeat the payment of a tax in two ways. He may attempt to cause an incorrect assessment of his tax liability to be made, by, for example, failing to report income. Or he may attempt to defeat the payment of a correctly assessed tax liability, by, for example, concealing assets. Here, the indictment charged petitioners with attempting to evade and defeat the payment of the tax by concealing the nature and extent of income from BIU's tax-return preparer and the IRS and by making false statements to BIU's accountant about BIU's income. Pet. App. 72a.

Petitioners contend (Pet. 13) that Section 7201 in effect states two different offenses, evasion of payment and evasion of assessment, and that they were charged with the former but convicted only on proof of the latter. The Court has never held, however, that Section 7201 states two different offenses, as opposed to one offense, a violation of which may be proven two (or more) different ways. In *Sansone*, the Court stated that Section 7201 "proscribes willfully attempting *in any manner* to evade or defeat any tax imposed by the Internal Revenue Code." 380 U.S. at 350 (emphasis added). The Court also stated that Section 7201 "includes the offense of willfully attempting to evade or defeat the *assessment* of a tax as well as the offense of willfully attempting to evade or defeat the *payment* of a tax," *id.* at 354, but it did not

suggest that those two theories of liability were actually distinct criminal offenses. To the contrary, the Court emphasized that either action would constitute a violation of Section 7201, and that a defense against one theory of criminal liability would not necessarily constitute a defense against the other. *Ibid.*

Petitioners argue (Pet. 15-19) that there is a conflict among the circuits on whether proof of evasion of payment of a tax requires proof that an assessment or other determination of tax has been made. Resolution of that asserted conflict, however, could not benefit petitioners. The court of appeals decided this case on the assumption that petitioners' reading of Section 7201 was correct.[2] Pet. App. 17a. Nonetheless, the

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[2] Although the court of appeals decided this case on that assumption, it is not clear that the court intended to adopt a definitive interpretation of Section 7201 in this case. Moreover, if the court is presented in a later case with a properly preserved challenge to a conviction of evasion for payment of taxes similar to the one in this case, it might well reconsider its assumption about the construction of Section 7201. The court relied on *United States* v. *England*, 347 F.2d 425, 430 (7th Cir. 1965), which it cited for the proposition that establishing evasion of payment requires proof of an assessment. *England*, however, has been significantly narrowed by the Seventh Circuit, which later explained "that *England* did not define a valid tax assessment as a necessary element of tax evasion in every case. Rather, *England* stands only for the proposition that where, under a peculiar set of facts, a valid tax assessment is a necessary element, the court cannot instruct the jury to find that element as a matter of law." *United States* v. *Dack*, 747 F.2d 1172, 1174 (7th Cir. 1984); see also *United States* v. *Dunkel*, 900 F.2d 105, 107 (7th Cir. 1990) ("Section 7201 creates only one *crime*: tax evasion. * * * Just as you can rob a bank in a dozen ways * * * so you can evade taxes in multiple ways."), vacated on other grounds, 498 U.S. 1043 (1991). Like

court affirmed petitioners' convictions on the ground that the indictment and the trial proceedings had put petitioners on notice of the theory of criminal liability under which the government was proceeding, and therefore petitioners were not prejudiced. *Id.* at 17a-18a. As the court of appeals pointed out (*id.* at 18a), a reading of the indictment as a whole made clear that the government intended to prove that petitioners evaded the payment of BIU's 1988 tax liability by preventing the correct assessment of it,[3] that petitioners were not surprised by the government's theory of the case,[4] and that the evasion count, Count 2, alleged conduct by the petitioners—concealment of income from the accountant who was preparing the tax return—that was relevant to evasion of the assessment of the tax. *Ibid.* The court of appeals' fact-bound conclusion that petitioners were in fact charged with evasion of assessment and suffered no prejudice at their trial on that charge is sufficient to

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the Seventh Circuit, the Ninth Circuit has held that proof of an assessment is not necessary to establish evasion of payment of taxes. *United States* v. *Voorhies*, 658 F.2d 710, 714-715 (1981).

[3] In its opening statement, the government informed the jury: "What is in dispute is whether these defendants intentionally and knowingly caused the income to be left off of the tax returns." C.A. Supp. App. 39a.

[4] In their opening statements, counsel for each petitioner described the case as involving evasion by preventing the correct assessment through omission of income from BIU's 1988 tax return. See C.A. Supp. App. 41a-42a ("[T]he government alleges * * * that one or more of the defendants in this case hid the existence of another BIU account * * * and as a result, certain income items were not included on the '88 return."); *id.* at 47a (petitioner Mark McLaughlin's counsel, telling the jury in his opening statement that "[t]he issue is, did they set out to cheat on their tax return").

dispose of any contention that there was plain error at petitioners' trial.

3. Petitioners contend that the lower courts should have suppressed evidence about the contents of corporate books and records voluntarily provided to the IRS by BIU's former accountant because (they argue) the IRS was required by 26 U.S.C. 7609 to issue a summons to the accountant and to provide petitioners with notice of that summons. That contention is without merit. Section 7602(a)(1) of Title 26 broadly authorizes the IRS "[t]o examine any books, papers, records, or other data which may be relevant or material" to an investigation into a taxpayer's tax liability. Section 7602(a)(2) further authorizes the IRS to issue administrative summonses to custodians of records to require the production of testimony and records. Section 7609(a) provides that, *if* a summons is issued to certain third-party recordkeepers, including banks, attorneys, and accountants, then the IRS must give notice to the affected taxpayer, and Section 7609(b) permits the taxpayer to petition the IRS to quash a summons issued to a third party.

Petitioners contend that Section 7609 provides the exclusive means by which the Internal Revenue Service may obtain records from a taxpayer's accountant. That reading of Section 7609 is unfounded. Section 7602(a) provides both an informal, noncompulsory means of obtaining information and a formal mechanism for the compulsory production of documents and testimony. See *Speck* v. *United States*, 59 F.3d 106, 108 (9th Cir. 1995). That broad discretionary authority to examine books and records is not limited by any requirement that the Internal Revenue Service first

issue a summons for such documents.[5] Nor is that broad authority limited by the restrictions of Section 7609. By the express language of the statute, the notice requirements of Section 7609 apply only "[i]f" a summons is served upon a third-party recordkeeper described in the statute. See 26 U.S.C. 7609(a)(1). Nothing in the statute prohibits the IRS from requesting access to such records informally, without the issuance of a summons. Moreover, the pertinent regulation of the Department of the Treasury provides that "Section 7609 does not restrict the authority under section 7602 (or any other provision of law) to examine records and witnesses without serving a summons and without giving notice of an examination." 26 C.F.R. 301.7609.1(a). That regulation, which is in accord with the plain language of the statute and reasonably implements it, is deserving of this Court's "customary deference" to Treasury Regulations. See *Commissioner* v. *Portland Cement Co.*, 450 U.S. 156, 169 (1981).

Contrary to petitioners' contention (Pet. 26-28), there is no conflict between the decision below and either *Neece* v. *IRS*, 922 F.2d 573 (10th Cir. 1990), or *United States* v. *Kao*, 81 F.3d 114 (9th Cir. 1996). *Neece* concerned whether a bank may voluntarily turn records over to the IRS without violating the Right to Financial Privacy Act (RFPA), 12 U.S.C. 3401 *et seq.* The RFPA generally prohibits financial

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[5] We are informed by the IRS that taxpayers and their accountants voluntarily provide information in the vast majority of IRS civil audits of income tax returns. Under petitioners' construction of Section 7609, however, the IRS could not obtain the records necessary to conduct a civil audit of any taxpayer who employed an accountant without first issuing an administrative summons.

institutions from producing bank records for the IRS except pursuant to certain procedures providing for notice to the bank customer and an opportunity for the customer to challenge production of the bank records. 12 U.S.C. 3402. The RFPA also provides that nothing in that Act "prohibits the disclosure of financial records in accordance with procedures authorized by Title 26." 12 U.S.C. 3413(c). In *Neece*, the court held that the exception in Section 3413(c) permitting disclosure of bank records to the IRS applies only when a summons is issued to a financial institution under Section 7609, and not also when the IRS makes an informal request to a financial institution for records about a customer under its Section 7602 authority to conduct informal investigations. See 922 F.2d at 578. The *Neece* court did not hold that Section 7609 deprives the IRS of authority to obtain information about taxpayers through informal procedures, and that decision has no application outside the context of financial institutions covered by the RFPA.

United States v. *Kao*, *supra*, is also irrelevant to the case at hand. In *Kao*, the Ninth Circuit held that Section 7602 does not authorize the IRS to compel taxpayers to execute consent directives that would enable the IRS to obtain records from third parties through means other than those established in Section 7609. See 81 F.3d at 116-117. *Kao* did not hold, however, that the IRS was prohibited from seeking the voluntary cooperation of third-party recordkeepers; moreover, the case specifically concerned the IRS's attempt to obtain information about the taxpayers from foreign banks, which might be barred by other countries' laws from voluntarily providing information about their customers. See *id.* at 117. *Kao*,

therefore, also has no application to the IRS's efforts to obtain information from accountants, who are not prohibited by federal law from voluntarily revealing tax information about their clients. See *Couch* v. *United States*, 409 U.S. 322 (1973).

Petitioners gain no support from a statement by Senator Haskell on the floor of the Senate, which, as petitioners note (Pet. 25 n.7), was cited as authority in *United States* v. *Mobil Corporation*, 543 F. Supp. 507 (N.D. Tex. 1981). Senator Haskell offered his interpretation of Section 7609 several days after the bill that contained that Section had been passed by the Congress. He stated that, although "[a]t no time did we discuss the questions of allowing informal access to these records without a summons of any sort[,] * * * [i]t seems to me absurd to suggest that the Congress would act so clearly to protect citizens from the processes of an agency and make those protections optional, binding only when the agency chose." 122 Cong. Rec. 34,772 (1976). That post-enactment statement, which represents only the view of a single Senator, is entitled to little weight. See *Bath Iron Works Corp.* v. *Director, Office of Workers' Compensation Programs*, 506 U.S. 153, 166 (1993); *Zuber* v. *Allen*, 396 U.S. 168, 186 (1969).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

SETH P. WAXMAN
Solicitor General
LORETTA C. ARGRETT
Assistant Attorney General
ROBERT E. LINDSAY
ALAN HECHTKOPF
WILLIAM A. WHITLEDGE
Attorneys

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